



California Public Employees' Retirement System
Office of Audit Services
P.O. Box 942701
Sacramento, CA 94229-2701
TTY: (916) 795-3240
(916) 795-0900 phone, (916) 795-4023 fax
www.calpers.ca.gov

May 24, 2011

Employer Code: 5157-5240
Job Number: P10-006

Office of the Inspector General
Renee V. Hansen, Chief of Administration
P.O. Box 348780
Sacramento, CA 95834-8780

Dear Ms. Hansen:

Enclosed is our final report on the results of the state agency review completed for the Office of the Inspector General. Your Department's written response indicates agreement with the issues noted in the report. The written response is included as an appendix to the report. As part of our resolution process, we have referred the issues identified in the report to the appropriate divisions at CalPERS. Please work with these divisions to address the recommendations specified in our report. It was our pleasure to work with your agency and we appreciate the time and assistance of you and your staff during this review.

Sincerely,

Original Signed by Margaret Junker
MARGARET JUNKER, Chief
Office of Audit Services

Enclosure

cc: Finance Committee Members, CalPERS
Peter Mixon, General Counsel, CalPERS
Darryl Watson, Chief, CASD, CalPERS
Mary Lynn Fisher, Chief, BNSD, CalPERS
Don Martinez, Interim Assistant Chief, HAS, CalPERS

Office of Audit Services



State Agency Review

Office of the Inspector General

OFFICE OF THE INSPECTOR GENERAL

TABLE OF CONTENTS

<u>SUBJECT</u>	<u>PAGE</u>
Results in Brief.....	1
Background.....	1
Scope.....	3
Risk and Mitigation Table.....	5
Exceptions	
Risk 5: Coverage Group.....	7
Risk 7: Health Documentation.....	9
Risk 8: ACES	10
Conclusion	11
Department's Written Response	Appendix

OFFICE OF THE INSPECTOR GENERAL

RESULTS IN BRIEF

We reviewed the Office of the Inspector General's (Department) enrolled individuals, health and retirement contributions, member earnings and required health, retirement and Automated Communications Exchange System (ACES) documentation for employees included in our test sample. A detail of the exceptions is noted in the Risk and Mitigation Table. Specifically, the following exceptions were noted during the review:

- An incorrect retirement account code was assigned for one individual.
- Required health benefit documentation was not on file for five members in our sample.
- Required ACES Employer User Security Agreement was not on file for four ACES users.

BACKGROUND

The California Public Employees' Retirement System (CalPERS) provides a variety of programs serving members employed by more than 2,500 local public agencies as well as state agencies and state universities. The agencies contract with CalPERS for retirement benefits, with CalPERS providing actuarial services necessary for the agencies to fund their benefit structure. In addition, CalPERS provides services which facilitate the retirement process.

CalPERS Customer Account Services Division (CASD) manages contract coverage for public agencies and receives, processes, and posts payroll information. CalPERS Benefit Services provides services for eligible members who apply for service or disability retirement. Benefit Services sets up retirees' accounts, processes applications, calculates retirement allowances, prepares monthly retirement benefit payment rolls, and makes adjustments to retirement benefits. Health Account Services provides eligibility and enrollment services to the members and employers that participate in the CalPERS Health Benefits Program, including state agencies, public agencies, and school districts.

State members include state miscellaneous, highway patrol, state safety, state industrial and state peace officer/firefighter (POFF) members. California Government Code (GC) § 20370 through § 20445, provides detailed definitions for these classifications. These classifications denote different retirement benefit formulas, which include: 2% at age 55 for state miscellaneous or industrial members (GC § 21354.1); 3% at age 50 for state patrol members (GC § 21362.2); 2.5% at age 55 for state safety members (GC § 21369.1); 3% at age 55 for POFF and local safety members (GC § 21363.1); and, 3% at age 50 for POFF members (GC § 21363.4 and § 21363.8).

OFFICE OF THE INSPECTOR GENERAL

Retirement allowances are computed using three factors: years of service, age at retirement and final compensation. Final compensation is defined as the highest average annual compensation earnable by a member during the last one or three consecutive years of employment, unless the member elects a different period with a higher average. State and school members use the one-year period. Local public agency members' final compensation period is three years unless the agency contracts with CalPERS for a one-year period.

Unlike contracting agency retirement benefit program operations, state agencies do not report member enrollment and monthly payroll data to CalPERS. Instead, each state agency inputs membership and payroll information with special designated codes into the Personnel Information Management System (PIMS) through Personnel Action Request forms. PIMS contains official personnel, payroll, and retirement information for state employees. The State Controller's Office (SCO) has the responsibility for maintenance and security of PIMS.

In accordance with the SCO's published Personnel Action Manual and Payroll Procedures Manual, state agencies input necessary personnel and payroll changes into PIMS. The system automatically passes data fields that are necessary for retirement benefit calculations to CalPERS via CalPERS' Transaction Log. The data from PIMS updates the appropriate CalPERS application systems, such as the Contribution Reporting System, Retirement Information Benefit System and CalPERS Online Member and Employer Transaction System. One critical data element passed on from state agencies to CalPERS, via the SCO, is the employee's Retirement Account Code (RAC). The RAC is a one or two digit alpha or numeric code used by PIMS to designate an employee's retirement status. During system updates from SCO to CalPERS, the RAC for each employee is converted to a coverage group code, which is significant for determining retirement contribution levels while the employee is active and the retirement formula when the employee is applying for retirement.

In general, when changes are mandated by law or contract, without the need for state agencies to prepare payroll change documents, payroll changes may be made automatically by the SCO. However, each agency has full responsibility for preparing accurate Personnel Action Request forms, employee attendance reports, and selecting appropriate compensation codes. California State Civil Service Pay Scales are published by the Department of Personnel Administration. SCO's Payroll Procedures Manual, Section G 105, outlines miscellaneous special compensation payment processing methods and whether they are subject to CalPERS for the purpose of retirement calculation. The SCO also has the responsibility for processing the health care contribution amounts for state employees and state agencies. Based on the information

OFFICE OF THE INSPECTOR GENERAL

contained in PIMS, the SCO identifies and remits the state's contribution and the amounts authorized by employees and annuitants to be deducted from their salaries or retirement allowances for payment of contributions.

The Department was established by the Legislature in 1994 to review the policies and procedures of the Youth and Adult Correctional Agency in conducting audits and investigations. In 1998 and 1999, the Legislature significantly expanded the Inspector General's responsibility for overseeing California's correctional agencies and transformed the Department into an independent agency reporting directly to the Governor.

SCOPE

As part of the Board approved plan for fiscal year 2010/2011, we reviewed the Department's payroll reporting and enrollment processes as these processes relate to the Department's health and retirement mandates with CalPERS. The objective of this review was limited to the determination that the Department complied with applicable sections of the California Government Code (Sections 20000 et seq.) and Title 2 of the California Code of Regulations and that prescribed reporting and enrollment procedures were followed. The on-site fieldwork for this review was conducted on July 21 through July 23, 2010.

The review period was limited to the examination of the records and processes from July 1, 2007 through June 30, 2010. To accomplish the review objectives, we performed the following:

- ✓ Reviewed the mandated requirements the Department had with CalPERS, correspondence files maintained at CalPERS, and employment agreements the Department had with its employees.
- ✓ Interviewed key staff members to obtain an understanding of the Department's personnel and payroll procedures.
- ✓ Reviewed the payroll transactions for sampled employees and compared the Department's payroll information with the data reported to CalPERS to determine whether the Department correctly reported compensation.
- ✓ Reviewed the Department's payroll information reported to CalPERS for the sampled employees to determine whether payrates were reported pursuant to public salary information.

OFFICE OF THE INSPECTOR GENERAL

- ✓ Reviewed the Department's enrollment practices pertaining to temporary employees, retired annuitants, and independent contractors to determine whether the individuals met CalPERS membership requirements.
- ✓ Reviewed the Department's classification of employees to determine whether the Department reported sampled employees in the appropriate coverage groups. The retirement account code, which is entered by the Department into the SCO system, is converted to the coverage group code when the information is reported to CalPERS.
- ✓ Reviewed the Department's calculation and reporting of unused sick leave balances for a sample of retiring employees.
- ✓ Reviewed employees and their dependents to determine whether the Department properly enrolled eligible individuals into CalPERS Health Benefits Program.
- ✓ Determined whether the Department maintained the required user security documents on file and reasonable security procedures were in place for ACES users.

OFFICE OF THE INSPECTOR GENERAL

RISK AND MITIGATION TABLE

In developing our opinions, we considered the following risks and mitigations. We also include our observations and recommendations.

RISK	MITIGATION & OBSERVATION	RECOMMENDATION
1. The Department may not accurately report compensation to CalPERS.	We reviewed payroll records and compensation reported to CalPERS for a sample of 11 employees over two service periods. The service periods reviewed were January 2009 (01/09-0) and January 2010 (01/10-0). We determined that compensation was accurately reported to CalPERS.	None.
2. The Department may not report payrates in accordance with publicly available salary schedules.	We reviewed payrates reported to CalPERS and reconciled the payrates to the Department of Personnel Administration's public salary information to determine whether payrates for the sampled employees were properly authorized and reported to CalPERS. The service periods reviewed were January 2009 (01/09-0) and January 2010 (01/10-0). We determined the Department paid and reported salaries pursuant to the authorized published salary information.	None.
3. The Department may not enroll all eligible employees into CalPERS membership.	<u>Temporary/Part-time Employees</u> We selected a sample of five temporary/part-time employees and examined the number of hours worked in fiscal years 2008/2009 and 2009/2010 to determine	None.

OFFICE OF THE INSPECTOR GENERAL

RISK	MITIGATION & OBSERVATION	RECOMMENDATION
3. The Department may not enroll all eligible employees into CalPERS membership. (continued)	<p>whether they reached or exceeded the 1,000 hour membership eligibility requirement and were timely enrolled, or whether they had prior membership and should have been enrolled upon employment by the Department.</p> <p>We determined the agency enrolled eligible employees timely and properly excluded temporary/part-time individuals from CalPERS membership.</p> <p><u>Independent Contractors</u></p> <p>The Department did not employ the services of independent contractors during the review period.</p>	None.
4. The Department may unlawfully employ retired annuitants.	<p><u>Maximum Hours Threshold</u></p> <p>We reviewed the hours worked for five retired annuitants in fiscal years 2008/2009 and 2009/2010 to determine whether individuals worked more than 960 hours in a fiscal year. Our sample testing revealed that no sampled retired annuitant exceeded the 960 hour threshold.</p> <p><u>Bona Fide Separation</u></p> <p>We determined that a bona fide separation from employment, per Government Code Section 21220.5, was</p>	<p>None.</p> <p>None.</p>

OFFICE OF THE INSPECTOR GENERAL

RISK	MITIGATION & OBSERVATION	RECOMMENDATION
<p>4. The Department may unlawfully employ retired annuitants. (continued)</p>	<p>not needed as the five sampled retired annuitants' ages exceeded the normal retirement age at the time they provided services.</p> <p><u>Unemployment Benefits</u></p> <p>We determined that the Department had a method in place to ensure that retired annuitants who received unemployment insurance compensation during the prior 12 month period were not reappointed.</p>	<p>None.</p>
<p>5. The Department may not appropriately report employees under the proper coverage group code.</p>	<p>We examined the appropriateness and accuracy of assigned retirement account codes (RAC). A RAC is defined by SCO's Personnel Action Manual, page 2.62.2a, as, "A one or two digit alpha or numeric code used by the Employment History Database system to designate an employee's retirement status."</p> <p>We tested a sample of six employees representing six RAC types used by the Department. We reviewed each sampled employee's RAC and verified whether the coverage group was consistent with the information in the CalPERS database.</p> <p>We determined the Department accurately assigned RACs in accordance with the SCO's Personnel Action Manual and CalPERS' State Handbook for each sampled</p>	<p>The Department should ensure appropriate RAC assignments so that each employee is reported under the proper coverage group code.</p> <p>The Department should work with CalPERS CASD to assess the impact of this incorrect reporting and determine what adjustments are needed.</p> <p>A confidential list identifying the employee mentioned in this section of the report has been sent to the Department and</p>

OFFICE OF THE INSPECTOR GENERAL

RISK	MITIGATION & OBSERVATION	RECOMMENDATION
5. The Department may not appropriately report members under the proper coverage group code. (continued)	<p>employee, except in one instance.</p> <p>The Department assigned one member a retirement account code TS, defined by SCO's Personnel Action Manual as appropriate for an industrial Alternate Retirement Program (ARP) member with social security/medicare (SS/Med) who is first employed by the State on or after January 1, 2007, in Bargaining Units 1, 3, 4, 7, 10 or 11 through 21 who contributes to ARP for the first 24 calendar months of employment. The related coverage group was 11598 with a three-year final compensation, as indicated by CalPERS' State Handbook.</p> <p>The proper account code is TP, defined by SCO's Personnel Action Manual as appropriate for an industrial ARP member with SS/Med newly hired to the State on or after August 11, 2004, who contributes to ARP for the first 24 calendar months of employment. The coverage group is 11599 with a one-year final compensation, as indicated in CalPERS' State Handbook.</p>	CalPERS CASD as an appendix to our draft report.
6. The Department may not accurately report unused sick leave balances for retiring CalPERS members.	We reviewed the unused sick leave balances for a sample of five retirees to determine whether the Department properly computed and reported the balances. We determined the Department accurately certified retiring members' unused sick leave balances to CalPERS.	None.

OFFICE OF THE INSPECTOR GENERAL

RISK	MITIGATION & OBSERVATION	RECOMMENDATION
7. The Department may not properly enroll eligible employees and their dependents in health benefits.	<p>We reviewed a sample of five employees to assess the health benefits eligibility and enrollment of members and their dependents. Our sample testing revealed the Department properly enrolled eligible employees and their dependents in CalPERS Health Benefits Program, except for the following:</p> <p>The Department did not have the required Declaration of Health Coverage (HB-12A) form on file for the five sampled employees.</p> <p>The HB-12A provides information on enrollment options and consequences for non-enrollment and is to ensure compliance with the Health Insurance Portability and Accountability Act (HIPAA). Effective January 1, 1998, each employee must sign the HB-12A when they are first eligible to enroll or when they make any change to their health coverage. This includes open enrollment changes, changing health plans when moving, adding or deleting a dependent, or canceling health benefits. The employer must provide the HB-12A at the time the employee requests enrollment or with the Health Benefit Plan Enrollment (HBD-12) form. The employer must also provide the employee a copy of the signed form and keep the original in the employee's file.</p>	<p>The Department must ensure that the proper member and dependent enrollment documentation is on file at the Department within 60 days from the date of our final report.</p> <p>Please send an email to: <i>HBB_Audit_Services@calpers.ca.gov</i> once the requested documentation is on file. The CalPERS Health Account Services may be contacted at (916) 795-3836 with any questions.</p> <p>A confidential list identifying the employees mentioned in this section of the report was sent to the Department and CalPERS Health Account Services as an appendix to our draft report.</p>

OFFICE OF THE INSPECTOR GENERAL

RISK	MITIGATION & OBSERVATION	RECOMMENDATION
8. The Department may not maintain appropriate ACES security procedures.	<p>We reviewed the security procedures for the Department's ACES users to determine whether reasonable security precautions were maintained and to determine whether the required security documents were properly completed and filed for ACES users.</p> <p>We determined the Department practiced reasonable security procedures to protect passwords and unauthorized access to ACES. However, the Department did not maintain Employer User Security Agreement (AESD-43) forms on file for one active ACES user and three inactive ACES users.</p> <p>CalPERS ACES Security procedures outlined on the CalPERS website at www.calpers.ca.gov require agencies to keep a signed copy of security documents on file for ACES users. An AESD-43 must be completed for each employee using CalPERS on-line access and be available to CalPERS upon request. Forms must be retained in a secure work site location of the employer, for the life of the Agreement and for two years following the deactivation or termination of the Agreement. CalPERS is to be notified immediately in the event that any of its sensitive or confidential information is subjected to unauthorized disclosure, modification or destruction.</p>	<p>The Department should work with CalPERS CASD to ensure that ACES user security agreements are completed, submitted and maintained.</p> <p>A confidential list identifying the individuals mentioned in this section of the report has been sent to the Department and CalPERS CASD as an appendix to our draft report.</p>

OFFICE OF THE INSPECTOR GENERAL

CONCLUSION

We limited this review to the areas specified in the scope section of this report. We limited our test of transactions to samples of the Department's payroll reports and personnel records. The sample testing procedures provide reasonable, but not absolute, assurance that these transactions complied with the California Government Code, except as noted above.

Respectfully submitted,

Original Signed by Margaret Junker
MARGARET JUNKER, CPA, CIA, CIDA
Chief, Office of Audit Services

Date: May 2011

Staff: Michael Dutil, CIA, Senior Manager
Diana Thomas, CIDA, Manager
Jacque Conway, CPA, CIA, Manager
Emma Shaw

APPENDIX

DEPARTMENT'S WRITTEN RESPONSE



May 1, 2011

Employer Code: 5157-5240

Job Number: P10-006

MARGARET JUNKER, Chief
Office of Audit Services
California Public Employees' Retirement System
PO Box 942701
Sacramento, CA 94229-2701

Dear Ms. Junker:

A draft report on your review of the Office of the Inspector General (OIG) was received on April 18, 2011. The OIG has reviewed the draft report and agrees with the recommendations. We have corrected the exceptions identified in Risks 5, 7, and 8.

We would like to thank Ms. Emma Shaw for her professionalism and thoroughness in conducting the audit. If you have any questions or concerns, call Elena Barbosa, at (916) 830-3631.

Sincerely,

A handwritten signature in black ink, reading "Renee V. Hansen", with a long, sweeping horizontal line extending to the right.

RENEE V. HANSEN
Chief of Administration (A)

cc: Bruce Monfross, Inspector General (A)
Mary Lynn Fisher, Chief, BNSD, CalPERS
Don Martinez, Interim Chief, EMHS, CalPERS